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227541

July 29, 2010

By Hand Delivery

Cynthia T. Brown, Chief
Section of Administration
Office of Proceedings
Surface Transportation Board
395 E Street, SW
Washington, D.C. 20423-0001

Re: Docket No. 42113, Arizona Electric Power Cooperative, Inc. v. BNSF Railway Company and Union Pacific Railroad Company

Dear Ms. Brown:

Enclosed for filing in the above docket on behalf of Complainant Arizona Electric Power Cooperative, Inc. ("AEPCO"), please find the following:

1. The original and twenty (20) copies of the Highly Confidential Version of AEPCO's Brief.

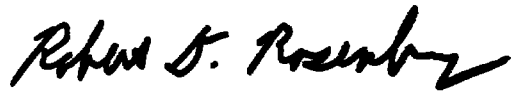
2. The original and ten (10) copies of the Public Version of AEPCO's Brief.

3. Three copies of a DVD containing electronic copies of the Highly Confidential Version of AEPCO's Brief.

Please note that this filing contains a page with color images, at the locations noted in the unbound originals.

Kindly date stamp the extra copies of this cover letter and the enclosed pleadings and return them to our messenger. Thank you for your attention to this matter.

Respectfully submitted,



Robert D. Rosenberg
An Attorney for Complainant Arizona
Electric Power Cooperative, Inc.

RDR:cej
Enclosures

cc: Counsel for Defendants BNSF Railway Company
and Union Pacific Railroad Company

PUBLIC VERSION

227541

BEFORE THE
SURFACE TRANSPORTATION BOARD

ARIZONA ELECTRIC POWER COOPERATIVE, INC.	
Complainant,	
v.	**Docket No. 42113**
BNSF RAILWAY COMPANY	
and	
UNION PACIFIC RAILROAD COMPANY	
Defendants.	

BRIEF OF COMPLAINANT
ARIZONA ELECTRIC POWER COOPERATIVE, INC.

ARIZONA ELECTRIC POWER
COOPERATIVE, INC.

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Dated: July 29, 2010

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ACRONYMS

The following acronyms and abbreviations are used:

AEO	2009 Annual Energy Outlook April Update Forecast
AEPCO	Arizona Electric Power Cooperative, Inc.
ANR	Arizona & Northern Railroad
Apache	Apache Generating Station
ATC	Average Total Cost
BNSF	BNSF Railway Company and Predecessors
CAPM	Capital Asset Pricing Model
CTC	Centralized Traffic Control
DCF	Discounted Cash Flow
EIA	Energy Information Administration
FED	Failed Equipment Detector
FRA	Federal Railroad Administration
G&A	General & Administrative
HDF	On-Highway Diesel Fuel Index
MMM	Maximum Markup Methodology
MOW	Maintenance of Way
MRL	Montana Rail Link
MSDCF	Multi-Stage Discounted Cash Flow
NPRB	Northern Powder River Basin
PRB	Powder River Basin
PTC	Positive Train Control
RTC	Rail Traffic Controller Model
SAC	Stand-Alone Cost
SARR	Stand-Alone Railroad
STEO	Short Term Energy Outlook
SWRR	Southwestern Railroad Company, Inc.
UP	Union Pacific Railroad Company
URCS	Uniform Railroad Costing System
WCTL	Western Coal Traffic League

CASE GLOSSARY

The following short form case citations are used:

AEP Texas	STB Docket No. 41191 (Sub-No. 1), *AEP Tex. N. Co. v. BNSF Ry.* (STB served Sept. 10, 2007)
AEP Texas 2009	STB Docket No. 41191 (Sub-No. 1), *AEP Tex. N. Co. v. BNSF Ry.* (STB served May 15, 2009)
AEPCO December 2001	STB Docket No. 42058, *Ariz. Elec. Power Coop. v. Burlington N. & S.F. Ry.* (STB served Dec. 31. 2001)
AEPCO August 2002	*Ariz. Elec. Power Coop. v. Burlington N. & S.F. Ry.*, 6 S.T.B. 322 (2002)
AEPCO March 2005	STB Docket No. 42058, *Ariz. Elec. Power Coop. v. Burlington N. & S.F. Ry.* (STB served March 15, 2005)
APS	*Ariz. Pub. Serv. Co. and PacifiCorp. v. The Atchison, Topeka and Santa Fe Ry.*, 2 S.T.B. 367 (1997)
Coal Rate Guidelines or Guidelines	*Coal Rate Guidelines, Nationwide*, 1 I.C.C.2d 520 (1985), *aff'd sub nom. Consolidated Rail Corp. v. United States*, 812 F.2d 1444 (3rd Cir. 1987)
Major Issues	*Major Issues in Rail Rate Cases*, STB Ex Parte No. 657 (Sub-No. 1) (STB served Oct. 30, 2006)
McCarty Farms	*McCarty Farms v. Burlington N. Inc.*, 2 S.T.B. 460 (1997)
Otter Tail	*Otter Tail Power Co. v. BNSF Ry.*, STB Docket No. 42071 (STB served Jan. 27, 2006)
PPL Montana	*PPL Montana, LLC v. BNSF Ry.*, 6 S.T.B. 752 (2003)
PSCo/Xcel I	*Public Service Co. of Colorado d/b/a Xcel Energy v. Burlington N. and Santa Fe Ry.*, 7 S.T.B. 589 (2004)
PSCo/Xcel II	STB Docket No. 42057, *Public Serv. Co. of Colorado d/b/a Xcel Energy v. Burlington N. and Santa Fe Ry.* (STB served Jan. 19, 2005).

TMPA	*Texas Mun. Power Agency v. Burlington N. and Santa Fe Ry.*, 6 S.T.B. 573 (2003)
WFA/Basin I	STB Docket No. 42088, *Western Fuels Ass'n, Inc. and Basin Electric Power Coop. v. BNSF Ry.* (STB served Sept. 10, 2007)
WFA/Basin II	STB Docket No. 42088, *Western Fuels Ass'n, Inc. and Basin Electric Power Coop. v. BNSF Ry.* (STB served Feb. 18, 2009)

BEFORE THE
SURFACE TRANSPORTATION BOARD

ARIZONA ELECTRIC POWER COOPERATIVE, INC.	)	
Complainant,	)	
v.	)	**Docket No. 42113**
BNSF RAILWAY COMPANY	)	
and	)	
UNION PACIFIC RAILROAD COMPANY	)	
Defendants.	)	

BRIEF OF COMPLAINANT ARIZONA ELECTRIC POWER COOPERATIVE, INC.

Complainant Arizona Electric Power Cooperative, Inc. ("AEPCO"), submits this Brief in support of its Complaint against Defendants BNSF Railway Company ("BNSF") and Union Pacific Railroad Company ("UP") (collectively, "BNSF/UP") for prescriptive rate relief and reparations for past overcharges for transportation of coal in unit trains from origins in New Mexico and the northern portion of the Powder River Basin ("PRB" or "NPRB") in Wyoming and Montana, including the Signal Peak Mine, to AEPCO's Apache Generating Station ("Apache") located near Cochise, AZ.

Consistent with Board precedent, AEPCO's Brief summarizes evidence and arguments on key issues without introducing new evidence.[1]

I. INTRODUCTION AND SUMMARY

AEPCO's rate case differs from most other coal rate cases in that it involves, among other things, two defendants, two origin areas, substantial guidance from AEPCO's prior rate case involving the same parties and origin areas, and a substantial volume of non-coal traffic in the SARR traffic group. In addition, AEPCO's SAC analysis, prepared in full compliance with the Board's orders in AEPCO's prior rate case and *Major Issues*, yields a MMM ratio that falls below not just the jurisdictional threshold, but slightly below 100% of variable cost, a result that is explained in large part by the presence of large volumes of so-called "competitive," but still very profitable, non-coal traffic.

What is more striking is the extent to which BNSF/UP's opposition departs from standard norms. BNSF/UP devote substantial effort in their Reply not to challenging AEPCO's SAC analysis, but instead to presenting their self-serving version of what they claim would constitute a proper SAC approach. That approach involves creating not just one, but two separate counter-SARRs (the ANR-NM and ANR-PRB) that fail the SAC analysis by design. The ANR-NM fails because it incorporates a *PPL Montana* cross-subsidy problem on the Deming-Rincon, NM segment, and the ANR-PRB

[1] AEPCO's Brief necessarily covers matters addressed in its Rebuttal submission, the most recent filing in the proceeding, which included a Counsel's Argument and Summary of Evidence as Part I. In the future, the Board may wish to stagger the briefs to reduce duplication and to advance the discussion.

fails because its costs exceed its revenues. The results are hardly surprising, as the last thing that BNSF/UP want to do is depict a least-cost, most-efficient railroad.

There is no need for AEPCO to adopt BNSF/UP's dysfunctional approach. AEPCO instead relies on the single SARR that AEPCO presented on Opening, the Arizona & Northern Railroad or ANR, that serves both origin areas on a least-cost, most-efficient basis, especially compared to BNSF/UP's approach. The relevant – and, effectively, the definitive – question is whether the ANR as configured by AEPCO complies with the Board's requirements, and it plainly does. The ANR conforms to the guidance that the Board provided in AEPCO's prior rate case, when it specifically said that: (a) AEPCO could route its movements of New Mexico coal via Vaughn, NM-El Paso, TX; (b) AEPCO could have the reasonableness of the PRB rates determined using a SARR that also handles the movements of issue New Mexico traffic; (c) a SARR can have internal traffic reroutes; and (d) a SARR may utilize trackage rights over third-party carriers. *See, e.g., AEPCO August 2002*, 6 S.T.B. at 324, 327, 329; *AEPCO March 2005* at 10-11. Recognition of these principles compels acceptance of AEPCO's configuration of its SARR.

Additionally, AEPCO's SAC presentation conforms to the Board's guidance in *Major Issues*, whereas BNSF/UP's approach does not, as exemplified by BNSF/UP's attempt to base the MMM analysis on an "ANR-URCS," ostensibly driven in part by the need to address a diverse (not all-coal) SARR traffic group, a matter that the Board explicitly addressed in proposing and adopting MMM in its *Major Issues* rulemaking proceeding. Furthermore, while BNSF/UP claim that AEPCO's SARR rests

upon improper cross-subsidies, they avoid even attempting to demonstrate that any segment of the ANR as configured by AEPCO fails under the *PPL Montana/Otter Tail* tests that the Board utilizes for determining if improper cross-subsidies are present.

Once it is recognized that AEPCO has properly configured the ANR, there is relatively little left to be decided. BNSF/UP challenge a number of aspects of AEPCO's calculation of the ANR's volumes, revenues, design, operating plan and expenses, road property investment costs, and DCF model, but BNSF/UP's claims are generally unfounded and in any event have relatively little impact on the SAC analysis, which still results in a MMM ratio well below the jurisdictional threshold.

Two issues relate to the calculation of the jurisdictional threshold. The first is that the SWRR should not be treated as an interline carrier because it serves as BNSF's sub-contractor and classifying the SWRR as an interline carrier transforms an arrangement that is intended to, and does, reduce the costs of the movement into one that nonsensically results in higher costs. The second is that there is no basis for calculating the jurisdictional threshold for the New Mexico movements based on the SARR routing, as only the actual routing can be properly utilized for that purpose.

Accordingly, the following table presents AEPCO's current calculation[2] of the maximum reasonable rates for the issue traffic:

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[2] The figures reflect estimated 2009 URCS unit costs based on the 2009 cost of capital as submitted by the Association of American Railroads. The Board may adopt a lower value based on the comments of the Western Coal Traffic League, of which AEPCO is a member.

Table 1
Maximum Rate Summary[1/]

Origin	1Q09	2Q09	3Q09	4Q09	1Q10
Lee Ranch	$10.12	$10.13	$10.48	$10.66	$10.94
El Segundo	$9.97	$9.99	$10.31	$10.51	$10.78
Gillette Area Mines (Eagle Butte)	$27.50	$27.54	$28.39	$28.87	$29.63
Spring Creek	$29.39	$29.45	$30.37	$30.89	$31.70
Decker	$29.27	$29.30	$30.22	$30.74	$31.55

[1/] The Maximum Rate Per Ton equals the greater of the Jurisdictional Threshold or MMM Rate per ton, which is the Jurisdictional Threshold in all instances.

Source: Rebuttal Table II-A-2 (AEPCO Rebuttal at II-5) and Rebuttal e-workpaper "Cochise MMM Rates Rebuttal.xls." No figure is shown for Signal Peak because that origin does not enter the SAC analysis until January 1, 2012.

In the remainder of this Brief, AEPCO will address individual issues, focusing on the key points that are of greater significance or magnitude. Failure to address any individual issue, or additional aspects of an issue, should not be construed as acquiescence to BNSF/UP's position.

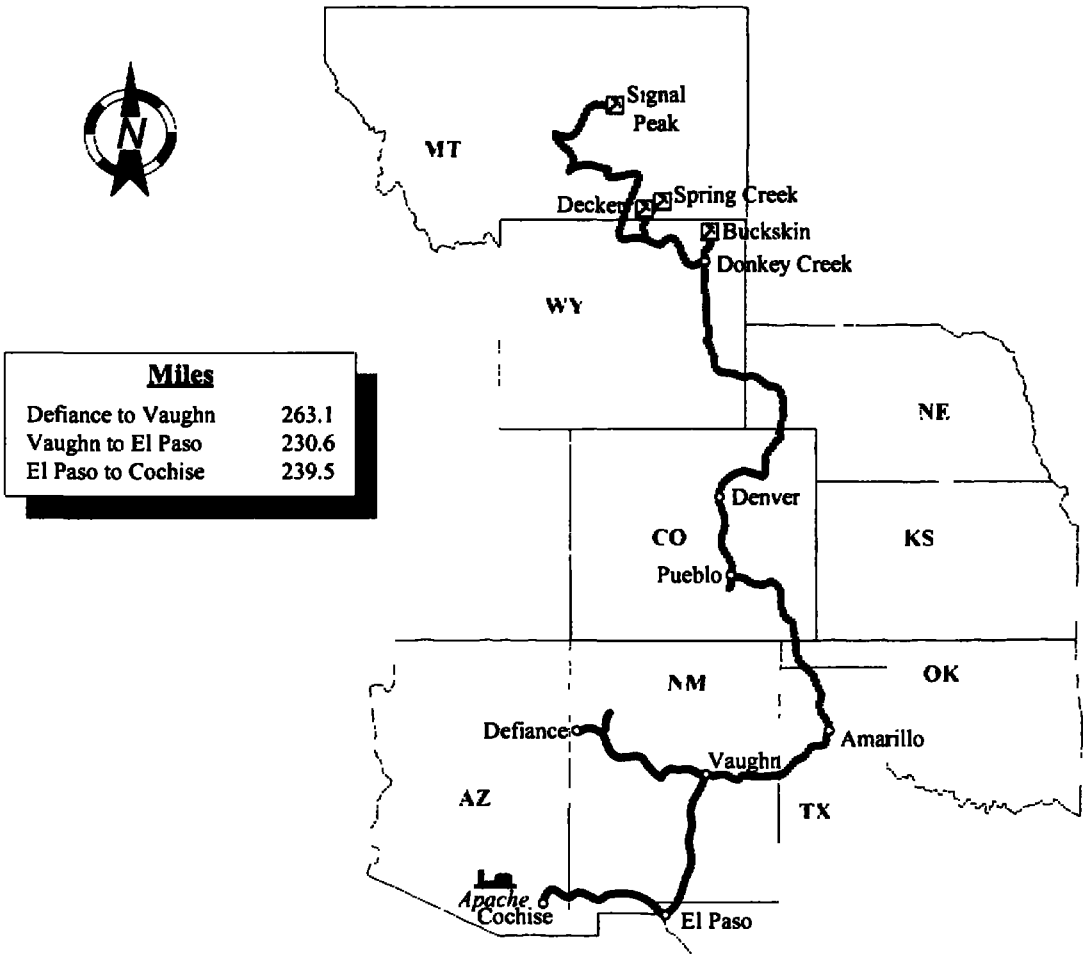
II. ANR CONFIGURATION AND TRAFFIC GROUP ISSUES (PART III-A)

A. AEPCO's Use of a Single SARR is Sound

As noted *supra*, BNSF/UP devote much of their Reply to their presentation of the separate ANR-NM and ANR-PRB. However, if AEPCO's use of a single SARR is accepted, as it must be, then BNSF/UP's presentation of the ANR-NM and ANR-PRB is rendered entirely irrelevant.

BNSF/UP's central claim is that AEPCO cannot use the portion of its SARR that handles the issue New Mexico traffic to handle the issue PRB traffic because the two portions supposedly have few facilities in common. *See, e.g.*, BNSF/UP Reply at III.A-6, citing *AEPCO 2002*, 6 S.T.B. at 329. However, the facts do not support BNSF/UP's claim, as shown by the following schematic:

Schematic Of The Arizona and Northern Stand-Alone Railroad



As shown, approximately two-thirds (64.1%) of the Defiance-Vaughn-El Paso-Cochise route miles used to handle the issue New Mexico traffic are also used to handle the issue PRB traffic. Specifically, the distance from Defiance to Vaughn is 263.1

miles, and the distance from Vaughn to Cochise via El Paso (used by both the issue New Mexico and PRB traffic) is 470.1 route miles.[3] As the bulk of the facilities used to handle the New Mexico issue traffic are also used to handle the PRB issue traffic, the central premise of BNSF/UP's cross-subsidization claim is unfounded, and their contention must be rejected.

Moreover, in AEPCO's earlier rate case, BNSF/UP's stated concern was that the PRB traffic would subsidize the New Mexico traffic,[4] and AEPCO's solution, which the Board approved, was to adopt a modular approach, under which the reasonableness of the PRB rates would be determined using a SARR that included the facilities utilized to transport the New Mexico traffic. *AEPCO August 2002*, 6 S.T.B. at 325. 329. AEPCO's single-SARR approach thus conforms exactly to what AEPCO proposed, and the Board approved, in AEPCO's prior rate case. Furthermore, requiring AEPCO to use two SARRs would prevent AEPCO from realizing the economies of density, scale, and scope that BNSF/UP enjoy in handling AEPCO's traffic and would thus constitute an impermissible entry barrier.

Furthermore, the Board has made clear that if a railroad wants to challenge a SARR configuration on the grounds that it presents a cross-subsidy, the railroad needs to proceed under the *PPL Montana/Otter Tail* tests:

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[3] The distances reflect those shown on AEPCO Opening Table III-B-2 at III-B-7, plus the additional 3.5 miles between Defiance and Vaughn added in AEPCO Rebuttal at III-B-7-8 and shown on AEPCO Rebuttal Exhibit III-B-1, p. 20.

[4] In other words, BNSF/UP's claim was that the segment from PRB to Vaughn would somehow subsidize the rest of the SARR.

> BNSF has failed to explain why the Board should not use its established test for detecting an impermissible internal cross-subsidy. Moreover, BNSF's approach is flawed because it does not permit the disputed traffic to make any contribution to unattributable operating costs. Having failed to identify any section of the SARR that is not self-supporting, BNSF has not met its burden to demonstrate that the SAC presentation rests upon an improper internal cross-subsidy. We will therefore include this disputed traffic in our analysis.

WFA/Basin I at 10. BNSF/UP are plainly aware of the Board's adoption of the *PPL Montana/Otter Tail* cross-subsidy tests, as they form the premise of BNSF/UP's design of and attack upon their ANR-NM. Under the circumstances, there is no basis on which to credit BNSF/UP's claim that the ANR as configured by AEPCO involves an impermissible cross-subsidy, as BNSF/UP failed to meet their burden to show that the ANR as presented by AEPCO contains any improper cross-subsidies.

BNSF/UP's position is thus contrary to both their prior position and the Board's prior decisions in AEPCO's previous rate case and elsewhere and must therefore be rejected.

B. AEPCO's Use of the Vaughn Connection is Sound

As part of its use of a single SARR, AEPCO routes both the issue New Mexico and issue PRB traffic through Vaughn and constructs appropriate connections at that location between the portions of the ANR system that replicate separate BNSF and UP facilities. AEPCO thus internally reroutes both the issue New Mexico and issue PRB traffic, consistent with established Board precedent. *See, e.g.*, AEPCO Opening at III-A-8-10.

However, BNSF/UP claim that AEPCO is required to replicate BNSF/UP's existing interchange points, *i.e.*, Deming for the New Mexico traffic and Pueblo, CO for the PRB traffic, and that AEPCO cannot utilize Vaughn to connect the replicated BNSF and UP line segments in any event because BNSF and UP do not have an existing interchange at that location. *See, e.g.*, BNSF/UP Reply at I-7-31, III.A-3, and III.A-7-8, 22-26. Of course, if AEPCO is required to use the separate Deming and Pueblo interchanges, then AEPCO would be required to present two SARRs.

There is no support for BNSF/UP's position. *Coal Rate Guidelines* makes clear that a shipper has "broad flexibility to develop the least costly, most efficient plant," that "an overriding factor may be the effort to lower costs by taking advantage of economies of density," and that the SARR "may not represent the shortest route for the captive shipper, but the one with highest traffic densities." 1 I.C.C.2d at 543-44. Insistence on replicating the incumbents' existing interchange would further violate the *Guidelines*, which give the shipper the right to configure its SARR as something other than a railroad, 1 I.C.C.2d at 543 & n.60, and preclude the SARR from utilizing internal reroutes in contravention of *PSCo/Xcel I*, 7 S.T.B. at 609, and other authority discussed in AEPCO Rebuttal at I-12-16 and III-A-17-27. Indeed, AEPCO's earlier rate case utilized the Vaughn-El Paso routing for all of the issue traffic. *AEPCO August 2002*, 6 S.T.B. at 327. BNSF/UP would effectively have joint rates adjudged under a more stringent SAC standard than for single-line rates, contravening Congress's clear statement in the Staggers Act Conference Report that "[t]he conferees intend that the rate

standard for the reasonableness of joint rates shall be the same as for all rates." H.R. Rep No. 96-1430 at 90 (1980).

BNSF/UP also claim in their Reply that AEPCO is precluded from altering their interchange (connection) points unless it brings a separate challenge to the through rate routing. BNSF/UP Reply at I-21-23. However, AEPCO need not challenge the existing routing in order to show that BNSF/UP's rate is too high. A SARR "stand[s] in the shoes" of the defendants, and acquires at least the same flexibility and discretion that they possess. *See, e.g., AEPCO March 2005* at 10-11. In AEPCO's earlier rate case, the Board reasoned that since "BNSF and UP are themselves free to alter or vary their routing of AEPCO's movements in this manner at any time (by mutually changing the interchange point) without needing AEPCO's consent and without affecting the joint rate charged to (and challenged by) AEPCO," AEPCO's use of a different routing and interchange "would seem to be permissible, so long as AEPCO had not specifically requested the routing that defendants currently use," which AEPCO did not do. *AEPCO August 2002*, 6 S.T.B. at 327.

BNSF/UP's claim that altering their interchange is inappropriate because they would need to alter their divisions must fail, as BNSF/UP's position during discovery was that their divisions on the issue traffic are irrelevant, an objection that the Board sustained in AEPCO's prior rate case. *AEPCO December 2001*, at 7; *see also Louisville & N. R.R. v. Sloss-Sheffield Steel & Iron Co.*, 269 U.S. 217, 234 (1925) (divisions irrelevant to the reasonableness of a joint rate); *Great Northern Ry. v. Sullivan*,

294 U.S. 458, 475 (1935); *Metropolitan Edison Co. v. Conrail*, 5 I.C.C.2d 385 (1989), and discussion in AEPCO Rebuttal at III-A-21-27.

AEPCO's use of Vaughn as the connection point between the BNSF and UP line segments replicated by the ANR is thus proper.

C. Utilization of MRL Trackage Rights

BNSF/UP object to AEPCO's use of trackage rights over Montana Rail Link ("MRL") between Laurel and Jones Junction. MT for non-issue traffic because some (not all) of that traffic does not use any other portions of the ANR's system that the ANR actually constructs. BNSF/UP Reply at III.A-18-21. However, AEPCO's use of the trackage rights is equivalent to BNSF's own use, and preventing AEPCO from utilizing BNSF's trackage rights over MRL under those circumstances would constitute an impermissible entry barrier. *See, e.g., AEPCO March 2005* at 10-11 ("allowing the SARR to have the benefit of the same trackage rights arrangement as the defendant railroad uses to move the traffic involved, at the same trackage rights fee, is necessary for the SARR to 'stand in the shoes' of the defendant"). AEPCO's use of the MRL trackage rights is thus entirely appropriate. AEPCO Rebuttal at III-A-27-31.

D. Other Trackage Rights Issues

AEPCO has constructed the Vaughn-El Paso segment of the ANR, thereby remedying what the Board viewed as the critical defect in AEPCO's prior rate case.

While BNSF/UP's ANR-PRB uses UP's trackage rights over BNSF between Pueblo and Stratford, TX, BNSF/UP Reply at III.A-13-14, AEPCO's ANR is not required to do so, particularly as the ANR's construction of that BNSF segment, as

well as the BNSF segment between Stratford and Vaughn via Amarillo, TX, produces a lower-cost, more-efficient configuration because of the density of the BNSF traffic, even after accounting for the additional costs associated with the longer routing. AEPCO Rebuttal at III-A-31-32. In particular, the ANR's RTC results are equivalent or superior to those of BNSF and UP in all material respects. *Id.* at III-C-40-42.

While the ANR replaces BNSF on the Denver-Pueblo and Pueblo-Vaughn segments, the ANR's traffic group includes some UP traffic that moves over these segments utilizing trackage rights. AEPCO has included this traffic for several related reasons explained in AEPCO Opening at III-A-11-14 and Rebuttal at III-A-33-41. First, UP traffic is included only if it actually moves over BNSF trackage. Second, AEPCO includes the UP traffic in its RTC simulation, which necessarily reflects treatment as if the ANR handles the traffic. Third, inclusion of the traffic enables the UP traffic to share in the MMM relief. If AEPCO treated the traffic as contributing only trackage rights fees, then the UP traffic would logically not share in the MMM relief. The participation in the MMM relief provides an appropriate incentive for UP and/or its customers to agree to the arrangement. Finally, the reciprocal trackage rights fees on the Denver-Pueblo segment do not reflect any capital ownership costs and thus do not reflect the true economic value of the trackage rights. Furthermore, AEPCO is not allowed to "stand in BNSF's shoes" on this segment, meaning that AEPCO would otherwise derive no benefit from the trackage rights arrangement on that segment, even though the arrangement benefits the defendants. Inclusion of the traffic, rather than the trackage rights fee, is thus the appropriate treatment for both segments.

E. The Board Should Prescribe PRB Rates

BNSF/UP contend in their Reply, at I-31-38, that the Board need not and should not prescribe rates from the PRB origins because AEPCO will supposedly not utilize those rates. However, AEPCO has already used the PRB rates, and its projections show sustained use of those rates {

}. AEPCO thus has a demonstrated need for the rates. In contrast, if rates are not prescribed, then BNSF/UP may seek to cancel the existing rates. The only real authority that BNSF/UP cite for their position is *AEP Texas 2009*. However, the Board declined to prescribe a rate reduction in that case only because any relief would have been in the last year of a 21-year DCF model and even that relief could disappear altogether if forecasts proved inaccurate. In contrast, AEPCO's DCF analysis shows that it is entitled to substantial relief (at the jurisdictional threshold) throughout the DCF model period. There is thus no basis for the Board not to prescribe rates or to relieve BNSF/UP from their obligation under 49 U.S.C. § 10701 and 10704 to maintain reasonable rates. AEPCO Rebuttal at I-16-21 and III-A-41-48.

F. Impact of the Recession on the ANR Volumes

In their Reply, BNSF/UP dispute at considerable length the level of volumes that AEPCO derived for its 2009 traffic group. Their principal contention is that AEPCO understates the decline in 2Q09-4Q09 volumes attributable to the recession. BNSF/UP Reply at III.A-28-31, 34-44.

AEPCO strongly disagrees. To develop its base year traffic group. AEPCO started with the most recent complete set of data – meaning revenue/waybill, car, and

train data – that both carriers provided, which covered the period from 2Q08-1Q09. To project 2009 volumes based on that data, AEPCO relied on a combination of BNSF/UP and publicly-available data and forecasts. AEPCO's approach is entirely reasonable and appropriate given the data made available by BNSF/UP. AEPCO Rebuttal at III-A-63-76 and 78-84.

While BNSF/UP claim to have selected an equivalent (but different) traffic group directly from the 2Q09-4Q09 data, their approach fails in numerous basic respects. First, BNSF/UP did not, and still have not, provided a complete set of revenue/waybill, car, and train data for any period after 1Q09. Without that data, their traffic selection cannot be verified, *e.g.*, neither AEPCO nor the Board can determine if the movements BNSF/UP included traverse the SARR, involve impermissible external reroutes, or if movements that were excluded should be included to benefit the SARR.

Second, BNSF/UP did not select an equivalent traffic group to that selected by AEPCO, but used various "shortcuts" that are inherently defective and designed to understate the available traffic group. For example, BNSF/UP purported to select BNSF intermodal trains with the same train symbols as those selected by AEPCO, but they did not include a particular train symbol unless AEPCO selected at least 90% of the trains with that particular symbol. BNSF/UP's effort to match 2Q09-4Q09 traffic to the 2Q08-4Q08 traffic selected by AEPCO also failed to account properly or fully for changes that occurred in the traffic between those two periods as various movements shifted or changed origins and/or destinations, as movements migrated from BNSF to UP or from UP to BNSF, and as the defendants gained new movements.

Third, while details of BNSF/UP's traffic group cannot be verified. it is clear that BNSF/UP's approach depicts, as BNSF/UP no doubt intend, a greater decline in traffic than BNSF/UP actually experienced in 2Q09-4Q09 relative to 2Q08-4Q08. Fourth, BNSF/UP's approach, which would effectively require AEPCO to "redo" its traffic group selection, is unworkable. AEPCO could begin the process only after the first year of operation of the DCF model had already elapsed. Even then, AEPCO could begin the process only after defendants produced a full set of data, and there would not be sufficient time for the rate case to be completed within the three-year period. Moreover, the defendants would then be in a position to exploit any decreases in revenues or volumes that might emerge in the second year of the DCF period by producing additional data. However, if the data showed better than expected growth, then the railroads would be free to decline to introduce that data. In this way, the defendants would be in a position to exploit their asymmetrical advantage in having control of the needed information.

Indeed, the defendants deploy that tactic against AEPCO in their Reply. While BNSF/UP devote great effort in attempting to depict a greater than forecasted decline in traffic for 2009, they make no effort to take into account the fact that their volumes in 2010 have experienced a greater than forecasted recovery and that recovery is expected to continue for the remainder of 2010. In other words, a balanced approach to updating would demonstrate that BNSF/UP's original forecasts remain reasonable over the long-term, even if they reflect a more linear trend than the actual short-term

operations show to date. BNSF/UP seek to adjust only for downward spikes, and they ignore the subsequent upturns, thereby "locking-in" a temporary decline for the remainder of the DCF period. The overall effect of their methodology is to skew the volume forecast trend downward for the entire model period. AEPCO Rebuttal at III-A-73-74 and 83-84.

Under the circumstances, BNSF/UP's approach cannot possibly be credited, and AEPCO's approach, which is sound and reasonable, especially in light of the data BNSF/UP produced, must be accepted as the best evidence of record.

G. Fuel Surcharges

Fuel surcharges account for a substantial portion of the rates charged by BNSF/UP, and fuel surcharges thus also account for a substantial portion of the ANR's revenues. The parties dispute two principal areas of fuel surcharges: (1) what traffic should be subject to the carriers' standard fuel surcharges, and (2) how the fuel surcharges should be calculated. BNSF/UP Reply at III.A-52-54, 59-61, 67-69, and 71-72; AEPCO Rebuttal at III-A-87-90, 94-96, and 101-07.

As to the first issue, BNSF/UP effectively claim that traffic that is not currently subject to their standard fuel surcharge programs will never become subject to the standard programs, and that the customers will instead effectively be able to rollover their contracts on the same basic terms, *i.e.*, they are effectively grandfathered out of standard fuel surcharges in perpetuity. BNSF/UP's claim is self-serving for their rate case purposes, but is untenable in light of their dedication to making all of their traffic subject to the fuel surcharges. It also cannot be reconciled with their representations to

the financial community that identify so-called "fuel cost recovery" as a vital area of revenue and margin growth. *See, e.g.,* Statements of Rob Knight, UP's Executive Vice President and Chief Financial Officer, quoted in AEPCO Rebuttal at III-A-104 ("Our legacy renewals also provide us with better fuel cost recovery.... We continue to make progress and you are right as we continue to clock off legacy contracts...."). There is no plausible basis on which to project that a significant portion of BNSF/UP's non-prescribed traffic will remain not subject to their fuel surcharge programs in the future as the current arrangements expire.

The second issue in calculating the fuel surcharge revenues involves the transition from projections of the retail price of highway diesel fuel ("HDF") in the Short Term Energy Outlook ("STEO") published by the Energy Information Administration ("EIA") to the long-term forecast in the long-term Annual Energy Outlook ("AEO") also published by the EIA. The STEO provides monthly forecasts that now run through the end of 2011, and the AEO provides annual forecasts that run to the end of the SAC DCF model. AEPCO and BNSF/UP both agree that the STEO should be used as long as possible, at which point the AEO governs. The AEO shows continuous annual increases, but the 2012 value is significantly lower than the December 2011 STEO value. BNSF/UP propose to simply switch from one forecast to the other in January 2012, thereby creating and exploiting an implicit price decrease that is inconsistent with both the STEO and AEO forecasts. AEPCO's approach is to calculate the percentage change in the AEO values from 2011 to 2012 and apply that percentage change to the twelve-month average of the STEO values for 2011, thereby reflecting the overall growth in the

AEO as applied to the more precise monthly estimates for 2011 contained in the STEO. AEPCO's method utilizes the additional monthly precision that is contained in the STEO forecasts and avoids the arbitrary decrease claimed by BNSF/UP. *See, e.g.*, AEPCO Rebuttal at III-A-88-90 and Rebuttal Exhibit III-A-3. AEPCO's approach thus constitutes the best evidence of record.

III. SARR CONFIGURATION AND MILEAGES (PART III-B)

Assuming that AEPCO's configuration of the ANR is accepted, as it must be for the reasons discussed above and in Part III-A-1 of AEPCO's Rebuttal, the parties' disagreements concerning route miles and track miles are very limited. As shown on AEPCO Rebuttal Table III-B-1 at III-B-28, AEPCO's route miles are 2.56 miles less than BNSF/UP's, its main-track miles are a net of 10.33 miles greater than BNSF/UP's, its helper pocket, setout, and MOW equipment tracks are 11.88 miles greater, its yard tracks are 3.3 miles greater, and its total track miles are 25.57 miles, or 0.71%, greater than those of BNSF/UP. AEPCO's mileages are tied to its operating plan, traffic group, and RTC simulation results, and AEPCO's mileages and configuration should thus be utilized as the best evidence of record, particularly given that the differences are so minor. A more complete discussion of the configuration/mileage differences between the parties is set forth in Parts III-B-1 and 2 of AEPCO's Rebuttal.

IV. SARR OPERATING PLAN (PART III-C)

Assuming, again, that AEPCO's configuration is accepted, as it must be, AEPCO's RTC simulation shows that the ANR provides transportation service equivalent or superior to that provided by BNSF/UP, notwithstanding the mileage increases resulting

from internal reroutes. AEPCO Rebuttal at III-C-40-42. The only potentially significant issues that arise as to the inputs for the RTC simulation relate to: (a) dwell times for coal trains at origins and destinations, (b) time allocated for track maintenance windows, and (c) time allocated for random track/signal and operating outages. Each is discussed below, as is (d) the results of the RTC simulation.

A. Dwell Times at Origins and Destinations

Consistent with Board precedent, AEPCO used actual average train dwell time for Wyoming mines served by the Orin Subdivision, Reno Branch, and Campbell Branch, primarily to account for interference from other trains (in particular UP trains that also serve the PRB "Joint Line" mines). This approach was accepted in *TMPA*, 6 S.T.B. at 654-55, and later utilized by both sides in *PSCo/Xcel*, *AEP Texas*, and *WFA/Basin I*.

For other origins and destinations served by the ANR, AEPCO generally used the maximum train loading and unloading free times specified in the applicable BNSF/UP pricing authorities for several reasons. First, there is no reason or basis to account for interference from other trains at these other locations. Second, the BNSF/UP data on train dwell times is suspect. For example, dwell times at one plant ranged from 0.0 hours to over nine days, and no explanation was provided for the variances. The longer dwell times might reflect the unrepresentative conditions present during 4Q08, when volumes were unusually high (especially compared to those during most of the base year). In addition, the pricing authorities leave, by design, a conservative time cushion for loading and loading at all locations, and the pricing authorities also provide for

compensation when the allowable free times are exceeded for reasons attributable to the fault of the customer or the mine. To the extent the trains exceeded the specified dwell times and there was no compensation, it appeared to be for the operational convenience of BNSF/UP, but there is no substantial reason for a SARR to seek to emulate such delays.[5] AEPCO Rebuttal at III-C-25-27. Under the circumstances, use of the maximum free times in the pricing authorities, except at the designated Wyoming origins, constitutes the best evidence of record, and AEPCO's approach should be accepted on this basis.

B. Planned Program Maintenance Outages During the Peak Period

In a departure from past practice, BNSF/UP claim that the RTC simulation should include outages for *planned* program maintenance activities that occur during the peak period. BNSF/UP Reply at III.C-38-39. However, a least-cost, most-efficient railroad would not schedule program maintenance for its peak period. Furthermore, there is no evidence that BNSF/UP actually scheduled program maintenance on any lines being replicated by the ANR during the base year peak period (October 8-22, 2008), and RTC simulations in past rate cases have not included program maintenance outages during the

[5] It may be that in the real world, BNSF/UP derive some benefit from delaying trains at origins or destinations. In particular, experienced dispatchers may well come to realize that delaying a train at an origin or destination may help mitigate congestion elsewhere on the system. However, the RTC software used in the simulation has virtually no ability to take advantage of such delays, *i.e.*, the software generally runs each train at the maximum possible speed until it reaches some congestion or choke point. Since the RTC simulation does not allow the SARR to realize such operational efficiencies associated with strategic delays, there is no reason to burden it with the costs (in this case, dwell times) associated with achieving those efficiencies.

peak period. *See, e.g., AEP Texas* at 17-21, and *WFA/Basin I* at 15-17. In addition, what BNSF/UP suggest constitute such outages are not adequately documented, but appear to constitute not program outages, but at most time allotted for inspections. {

} AEPCO Rebuttal at III-C-32-34. AEPCO's approach constitutes the best evidence of record in this aspect as well.

C. Random Outages

The nature of the dispute over random outages varies according to whether the real-world segments replicated by the ANR belong to BNSF or UP.

BNSF produced information regarding random outages on its segments in the base year, BNSF/UP Reply at III.C-39-41, but its information is sketchy. In particular, BNSF's information identifies just a particular event at a particular location, and not necessarily by individual track, as in some instances the same outage was reported twice when there were two tracks at the particular location. Furthermore, the BNSF information does not identify whether the event actually caused any disruption at the time or the extent of any disruption to train operations, *e.g.*, whether it involved just an inspection of such event, a slow order, or a partial outage.

While BNSF thus provided no information concerning the extent of actual disruption of its operations in the base year peak period. BNSF/UP generally assumed the "worst case scenario" in depicting the impact of the events in their RTC simulation for the peak period in 2018. In contrast, AEPCO's expert witnesses reviewed each event to

determine its likely impact, as reflected in AEPCO Rebuttal e-workpapers "BNSF outage data.pdf" and "RTC Reply Form B "0" Outages.xls" and discussed in AEPCO Rebuttal at III-C-34-38.

For example, BNSF/UP's RTC simulation depicted several switch problems that clearly affected only one of two main tracks in the area involved as halting all operations along both main tracks. One such incident is discussed in AEPCO Rebuttal at III-C-36-37. In addition, BNSF/UP depicted various reported incidents that were relatively minor in nature as causing rail operations in the area to come to a complete halt. Examples include dispatcher lost train ID (in CTC territory), office software problem (signal tested and train operations through the area monitored), FED (detector) axle count incorrect, track short circuit that cleared itself after it stopped raining, problems with switch heaters or gas snow melters that affected switches to industry leads. *etc*. AEPCO does not suggest that a prudent railroad operator would ignore such events, but would instead investigate them to determine their nature and especially their potential to disrupt safe operations. However, many of the events are not, based on the limited information recorded in the BNSF logs produced to AEPCO, sufficient to force the service outages depicted in BNSF/UP's RTC simulation, especially since there is no record that the events actually resulted in the outages depicted by BNSF/UP. Additional details on how AEPCO treated the outages that BNSF/UP included in their RTC simulation are provided in AEPCO Witness Reistrup's summary included in Rebuttal e-workpaper "BNSF outage data.pdf."

The net result of AEPCO's review of the BNSF data was to include a total of 108 outages on the BNSF-replicated segments in the Rebuttal RTC simulation. AEPCO's approach reflects outages and disruptions to the extent appropriate in each instance, and constitutes the best evidence of record.

In contrast, UP did not produce any useable information regarding "random" or other outages on its segments, and BNSF/UP did not include the impact of any such UP outages in their RTC simulation for the "Reply ANR" (their equivalent of AEPCO's single SARR). Nonetheless, BNSF/UP claim that the outages experienced on the BNSF segments should somehow be imputed to the ANR's UP segments. BNSF/UP Reply at III.C-42. There is no basis for such imputation, as doing so would be an exercise in sheer speculation given UP's failure to produce any data regarding actual events and/or their effect on train operations in response to AEPCO's discovery requests. AEPCO Rebuttal at III-C-38-39. Under the circumstances, there is no valid basis on which to impute any random outages on the UP segments.

D. Results of RTC Simulation

AEPCO's Rebuttal RTC simulation shows that the ANR peak-period 2018 transit times for all categories of traffic are generally comparable or superior to those experienced by BNSF/UP in the base-year 2008 period. The only significant exception is for the single loaded coal train moving from Lee Ranch Mine, NM to Apache, which has a hypothetical { }-hour increase in transit time. While a single train is not necessarily representative. AEPCO is certainly willing to accept the longer transit time in exchange

for the substantial reduction in rates that the ANR provides. AEPCO Rebuttal at III-C-40-42.

AEPCO's RTC simulation rests on a more credible set of inputs than does BNSF/UP's RTC simulation, and the Board should utilize AEPCO's RTC simulation as reflecting the best evidence of record. That said, AEPCO recognizes that the RTC simulation reflects a panoply of inputs, and changing those inputs (*e.g.*, removing movements from the traffic group, increasing dwell times or the delay associated with a random outage, *etc.*) has the potential to alter the results of the RTC simulation. Since the MMM ratio produced by the SAC DCF analysis is so far below the jurisdictional threshold, the Board may reasonably conclude that alteration of the inputs is unlikely to result in a material alteration of the SAC analysis.[6]

V. SARR OPERATING COSTS (PART III-D)

BNSF/UP claim that the ANR's 2009 operating expenses will be $1,113.3 million, over 30% greater than the $855.3 million that AEPCO presents on Rebuttal. BNSF/UP Reply at III.D-2; AEPCO Rebuttal at III-D-3. The three largest areas of dispute involve maintenance-of-way ("MOW"), Locomotive Operations (especially fuel costs), and General & Administrative ("G&A"), especially staffing.

[6] However, if the Board should decide that the inputs need to be altered and new RTC simulations prepared, then the parties should be given the opportunity to submit limited additional evidence utilizing the Board-specified inputs, consistent with the Board's approach in *AEP Texas* (STB served March 17, 2006), and *WFA/Basin* (STB served March 17, 2006). *See* AEPCO Rebuttal at I-35-36.

AEPCO's MOW plan, as clarified and revised on Rebuttal at III-D-124-156, avoids the extensive reliance on cross-training and outsourcing that has been problematic in past rate cases such as *AEP Texas* at 67-68. AEPCO's MOW plan relies on a substantial in-house staff of field employees to perform all maintenance except for program maintenance (large-scale rail and tie replacements, *etc.*) and certain other maintenance actives, such as rail grinding, that are more appropriately performed by a contractor due to their size and relative infrequency. AEPCO's MOW plan thus entails adequate staffing and constitutes the best evidence of record.

In their Reply, BNSF/UP also advance a novel claim that an additive – amounting to 35% of their proposed MOW costs – is required because AEPCO does not include improved maintenance or access roads along the ANR's tracks, which will supposedly cause maintenance crews to spend more time traveling to work areas on the tracks via hi-rail equipment. BNSF/UP Reply at III.D-93-94 and 121-131. The Board has held on several occasions that a SARR need not build construction or maintenance roads where the incumbent did not build them as part of the original construction. *See TMPA*, 6 S.T.B. at 701-02; *AEP Texas* at 80; *WFA/Basin I* at 83-84. BNSF/UP's additive rests on unproven and unsupported assumptions about the impact of improved maintenance roads, particularly the assertion that MOW crews will lack adequate track access without such roads. As explained in AEPCO Rebuttal at III-D-131-134 and 152-156, the ANR's MOW personnel will enjoy the same access to its tracks that BNSF/UP presently have on the vast majority of their lines being replicated by the ANR. If improved maintenance roads actually had the MOW productivity benefits claimed by

BNSF/UP, they would be a standard railroad feature, but they are manifestly not. BNSF/UP's proposed additive should be rejected.

A significant dispute between the parties as to locomotive operations involves fuel costs, particularly the delivered cost of diesel fuel at the ANR's West Vaughn and West El Paso inspection/fueling yards in New Mexico. BNSF/UP claim that AEPCO's use of BNSF's average delivered cost of fuel at its Belen, NM yard for the ANR's West Vaughn and West El Paso locations is improper because it does not account for additional transportation costs. BNSF/UP Reply at III.D-6-11. AEPCO's Rebuttal at III-D-6-17 explains that use of BNSF's figure is conservative because (a) diesel fuel could be delivered directly to West Vaughn by pipeline at a lower delivered cost, and (b) the cost at West El Paso would also be lower by using UP's pipeline-delivered cost at El Paso, even after accounting for the cost of transfer by tank car to West El Paso. AEPCO has thus actually overstated the delivered cost of fuel at both locations. BNSF/UP also dispute AEPCO's calculation of gallons of fuel consumed per locomotive unit mile ("LUM"). On Rebuttal, AEPCO adjusted its calculation, using data provided by BNSF/UP on Reply. to reflect BNSF average fuel consumption factors for the specific type of road locomotive used by the ANR. AEPCO Rebuttal at III-D-18-20.

The parties also differ as to the ANR's road locomotive requirements, which affects both lease costs and LUMs. The principal dispute involves the number of locomotives required for PRB coal trains that operate to/beyond Pueblo, CO. AEPCO equips these trains (like almost all of the ANR's other coal trains) with three locomotives in a distributed power or DP configuration and provides for assistance by helper

locomotives at two locations (one in Wyoming and one in Colorado). BNSF/UP propose to equip these trains with four locomotives over the entire distance operated, thus eliminating the need for helpers. AEPCO's Rebuttal at III-C-6-7 demonstrates that using helpers for short distances at the two locations is more efficient than requiring these trains to carry an extra road locomotive for several hundred miles (or more) in each direction. BNSF/UP have not demonstrated that this aspect of AEPCO's operating plan (and the associated locomotive operating expenses) is infeasible in any way, and AEPCO's plan should be accepted.

BNSF/UP's proposed G&A costs, BNSF/UP Reply at III.D-32-77, are also wildly overstated. In particular, BNSF/UP propose 315 G&A employees, which is almost *five* times the highest G&A staffing (66 employees) that the Board has previously accepted. *AEP Texas* at 51-53. BNSF/UP's staffing "evidence" generally consists of unsupported opinion testimony. In contrast, AEPCO's G&A Rebuttal at III-D-47-118, sponsored by four experts, including Dr. Patricia Buhler, a business school professor and widely-recognized expert on best practices in corporate management, demonstrates in detail why BNSF/UP's G&A evidence must be rejected, and why AEPCO's evidence (including the modest staffing increase provided on Rebuttal) should be accepted by the Board as the best evidence of record.

VI. SARR ROAD PROPERTY INVESTMENT (PART III-F)

AEPCO's Rebuttal road property investment figure is $6.81 billion or roughly $3.0 million per route mile. AEPCO Rebuttal Table III-F-1 at III-F-3 (as corrected in AEPCO's Errata filing of July 13, 2010). This figure compares favorably

with that in other recent Western SAC cases such as the $2.4 million per route mile in *AEP Texas 2009* and the $2.9 million in *WFA/Basin II*. In contrast, BNSF/UP posit road property costs of $8.24 billion, BNSF/UP Reply Table III.F.1 at III.F-2, almost 21% higher than AEPCO's figure on Rebuttal, and considerably higher on a route mile basis than in *AEP Texas 2009* and *WFA/Basin II*. On that basis alone, AEPCO's approach constitutes the best evidence of record.

Two areas, (a) earthwork unit costs and (b) ballast and subballast unit costs and related transportation costs, account for much of the difference between the parties' road property investment figures and are also representative of other disputed items. These two areas are summarized below.

BNSF/UP base their common earthwork unit cost on the Means Handbook, whereas AEPCO based its unit cost on actual BNSF projects undertaken on the lines replicated by the ANR. BNSF/UP Reply at III.F-5; AEPCO Rebuttal at III-F-4-6, III-F-23-29. Reliance on unit costs based on experience with actual projects has been accepted in other rate cases, such as *WFA/Basin I* at 86. Indeed, one of the projects that AEPCO incorporated into its common earthwork unit cost is the project utilized in *WFA/Basin I* at 82, 86.

BNSF/UP seek to impeach AEPCO's reliance on BNSF's actual costs by claiming that the projects are not representative of the ANR because the projects all occurred in Wyoming and/or reflected the alleged savings of constructing a second main track rather than a first main track. BNSF/UP Reply at III.F-20-23. Neither criticism is valid. For example, the BNSF construction projects relied upon by AEPCO include one

project located near Amarillo, TX, besides which BNSF/UP have provided no explanation as to why costs would be any lower in Wyoming. Nor have BNSF/UP shown that there are any actual savings associated with constructing second main track as opposed to the first main track. For example. the presence of an existing track may impede access to the location of the second track, and the construction activities would otherwise need to avoid disruption to traffic on active lines as well as damage to those lines. Both of these factors logically increase, rather than decrease, the costs of second main construction. AEPCO Rebuttal at III-F-23-27. BNSF's contentions thus rest on empty speculation, and AEPCO's approach constitutes the best evidence of record.

Regarding ballast costs, AEPCO on Rebuttal made two modifications in response to arguments raised by BNSF/UP by adding an additional quarry to supply ballast and correcting and/or modifying the mileages used to develop the transportation costs for the ballast. AEPCO provided extensive details supporting its revisions. AEPCO Rebuttal at III-F-58-61. BNSF/UP, in contrast, provided no detailed calculations of its delivered cost of ballast. Instead, BNSF/UP simply included a hard-coded average ballast cost that exceeds AEPCO's rebuttal weighted average delivered cost of ballast by $6.00 per ton. *Id.* at III-F-60-61. AEPCO's approach again constitutes the best evidence of record.

Similar issues arise regarding subballast. In particular, AEPCO on Rebuttal included additional sources and corrected and/or modified its transportation costs, but rejected BNSF/UP's attempt to discredit their own documents on subballast costs produced in discovery (BNSF/UP Reply at III.F-5-6), their attempt to increase subballast

transportation costs by using extremely circuitous routes, and their first-time claim that subballast moving by rail would have a higher rejection rate than subballast moving by truck and thus could not be utilized. when their own documents show otherwise. *See* AEPCO Rebuttal at III-F-61-64. The Board has previously stated that "parties must be able to rely on information supplied in discovery" in ruling that "BNSF may not impeach that information." *PSCo/Xcel I*, 7 S.T.B. at 673. 683 (rejecting evidence based on a letter from an employee that BNSF filed just before it submitted reply evidence). BNSF/UP have thus failed to undermine AEPCO's calculations, and AEPCO's calculations must be accepted as the best evidence of record.

Another area of disputes involves whether to include capital costs associated with Positive Train Control ("PTC"). BNSF/UP Reply at III.F-95-96; AEPCO Rebuttal at III-C-49-51 and III-F-75. BNSF/UP seek to include $88 million in additional road property investment costs to account for PTC investment based upon what UP projects to spend to meet the 2015 PTC implementation requirements. as applied to the ANR. AEPCO included costs for staff to implement PTC,[7] but explained that attempting to calculate the capital compliance costs is necessarily speculative at this time, especially as significant issues remain as to how the Federal Railroad Administration ("FRA") will interpret the PTC requirements, whether the railroads will obtain any tax breaks or other benefits to cover the costs of PTC implementation, and whether the railroads will be

[7] AEPCO's Operating Plan for the ANR provides for staffing for an inter-departmental PTC Compliance Group consisting of six positions (a Director, four professional staff members, and a full-time administrative assistant). AEPCO Opening at III-C-60 and III-D-19-20 and AEPCO Rebuttal at III-C-49.

successful in delaying PTC implantation, *etc.* In STB Docket No. 42114, *US Magnesium, L.L.C. v. Union Pacific R.R.* (STB served Jan. 28, 2010), a small shipper rate case involving the Three-Benchmark standard, the Board agreed that "there is a great deal of uncertainty surrounding PTC investment," and found that "UP has not demonstrated the precise amounts that could be reasonably ascribed to USM's traffic." *Id.* at 17. On that basis, the Board decided that it was premature to include PTC costs:

> While we understand that the costs of PTC might be significant and that carriers might need to recover the additional costs from their customers in the future, the adjustment advocated by UP cannot be justified here.... UP has not demonstrated here that PTC investments are sufficiently defined such that UP can quantify its costs or fairly attribute those costs to USM's traffic.

Id. at 2. The same limitations prevent the imputation of PTC costs here. However, even if BNSF/UP's figure were included in full,[8] it would not materially alter the SAC DCF analysis.

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[8] BNSF/UP's calculation is suspect and even self-contradictory. In particular, BNSF/UP simultaneously assert that (a) the ANR's hardware cost will be the same as that for all of UP, but (b) the ANR's track-related unit costs need to be increased by 50% because the ANR will not achieve UP's economies of scale as the ANR is only 6.85% the length of UP. As for (a), a system that is only one-sixteenth as large should not have the same hardware requirements. Moreover, items such as PTC systems are often sold on a "value-added" basis, and vendors would thus not expect to charge an entity such as the ANR the same price as they would charge a much larger entity such as UP. Furthermore, any vendor that has delivered or produced at least one PTC system will benefit from savings in delivering an additional system, and other vendors that have not actually delivered systems will need to price their offerings accordingly. In addition, BNSF/UP's increase for the economy of scale adjustment for (b) is counter to SAC theory. Indeed, defendants elsewhere (*e.g.*, G&A requirements) stress the size of the ANR, which suggests that the ANR would be sufficiently large to realize economies of scale and certainly would not need to pay 50% more per-mile for integration and testing.

VII. DCF ANALYSIS (PART III-G)

Disputes over the DCF analysis are limited to several discrete issues.

BNSF/UP object to AEPCO's exclusion of the 2008 MSDCF component of the cost of equity, BNSF/UP Reply at III.G-1-5, but the MSDCF calculation rests on growth assumptions that do not apply to the ANR. AEPCO Rebuttal at III-G-1-2. While BNSF/UP claim that the lack of growth will be offset by higher cashflows, the MSDCF analysis hinges on the relationship of the cashflows, the growth rate, and the stock price (or market capitalization). However, the ANR has no stock price or appropriate surrogate and the DCF cashflows cannot be appropriately compared to those under the MSDCF model. AEPCO Rebuttal at III-G-3-12. Moreover, while BNSF/UP claim that AEPCO is required to use the Board's COE calculation as is or not at all, BNSF/UP themselves seek to augment the Board's figure with a flotation cost additive ostensibly based on that in *AEP Texas*, BNSF/UP Reply at III.G-2. 5-8. Their *AEP Texas* analogy is inapposite as the ANR does not propose to engage in the refinancing that provided the predicate for inclusion of the flotation cost additive in that case. In addition, the additive that BNSF/UP seek is thirty times the additive allowed in *AEP Texas* under the unique circumstances of that case. AEPCO Rebuttal at III-G-12-15. AEPCO's approach to the COE thus constitutes the best evidence of record.

BNSF/UP also seek to modify AEPCO's approach to indexing land values, BNSF/UP Reply at III.G-8-12, but their approach devolves to using a two-year average that just happens to track a substantial and unusual decrease in real estate values. AEPCO Rebuttal at III-G-16-20. In contrast, AEPCO's use of a longer measuring period

is consistent with Board precedent, *e.g.*, *APS*, 2 S.T.B. at 440, and *McCarty Farms*, 2 S.T.B. at 523, and constitutes the best evidence of record.

BNSF/UP also seek modifications of the standard 10-year DCF model that the Board prescribed in *Major Issues*, BNSF/UP Reply at III.G-12-19. but the modifications involve matters that should have been presented in the *Major Issues* rulemaking, if at all, especially as BNSF/UP acknowledge that the problem (to the extent there is one) was presented as early as *APS*, 3 S.T.B. at 82-83, in 1998. Beyond that, their modifications are one-sided. If their requested modifications were to be made, then it would be necessary to make adjustments for additional gains in operating expense productivity that the ANR would experience after the initial 10 years of the DCF model as well as gains in capital asset productivity that the Board itself noted in *Major Issues*. AEPCO Rebuttal at III-G-20-24. Again, AEPCO's approach constitutes the best evidence of record.

VIII. RESULTS OF SAC ANALYSIS (PART III-H)

AEPCO's SAC analysis results in a MMM ratio that is not only below the jurisdictional threshold, but actually below 100% of variable costs in all years of the DCF model. AEPCO Rebuttal Exhibit III-H-4. The SAC analysis thus provides a substantial cushion in that most of the reductions in revenues and increases in costs that BNSF/UP seek could be adopted, yet AEPCO would still be entitled to a rate set at the jurisdictional threshold. As explained at the outset, this reality provides the impetus for BNSF/UP to

depart from standard railroad practice and present alternate SARRs and associated SAC analyses in order to avoid the results of AEPCO's single/combined SARR analysis.[9]

While BNSF/UP elsewhere suggest that a MMM ratio below 100% is so inherently suspect as to be "nonsensical," BNSF/UP Reply at I-5, the fact is that the ANR begins with a traffic group with an average revenue-variable cost ratio of only 136%.[10] This relatively low starting ratio confirms the reasonableness of the MMM result. In particular, a substantial part of the ANR's traffic group consists of intermodal traffic, which is generally deemed to have a relatively low revenue-variable cost ratio. *Id.* In order for this traffic to share in the MMM savings, the MMM ratio must be correspondingly low. In this respect, the MMM results are entirely logical and appropriate, and not "anomalous" as claimed by BNSF/UP in their Reply at I-6.

Notwithstanding their claims that premising a SARR on so-called competitive traffic is anomalous, BNSF/UP propose that MMM relief should be allocated not on the basis of the Phase III URCS variable costs of BNSF and UP, but instead on the variable costs of the ANR itself, which BNSF/UP purport to derive using the Phase III URCS as applied to the ANR DCF analysis (what they designate as their "ANR-URCS"). BNSF/UP Reply at III.H-8-17. This attempt is flawed in numerous respects, as explained in AEPCO Rebuttal at III-H-9-22. First, it is directly contrary to the Board's statements

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[9] In addition, the low ratio obviates the basis on which the Board declined to prescribe a rate in *AEP Texas 2009*, which is BNSF/UP's ostensible predicate for claiming that the Board should not prescribe a rate for AEPCO's PRB movements.

[10] The ANR has ATC divisions of $2.075.8 million and total Phase III variable costs of $1.523.9 million. *See* AEPCO Rebuttal e-workpaper "ANR MMM Model Reb.xlsx," cells G214286 (revenues) and I214286 (variable costs).

in *Major Issues*, AEPCO's prior rate case, and elsewhere that the purpose of the SAC exercise is to determine the extent to which the defendant(s), and not the SARR, has overcharged relative to its variable costs. Second, BNSF/UP's approach also contravenes the Congressional directive that joint rates are to be adjudged under the same standard applicable to single-line rate. H.R. Rep No. 96-1430 at 90 (1980). Third, the ultimate effect of BNSF/UP's approach is simply to shift costs from non-coal traffic to coal traffic, including the issue traffic, in derogation of the Board's insistence in *Major Issues* and elsewhere that MMM and variable costs be based on Phase III URCS costs. In other words, BNSF/UP seek to make the intermodal traffic appear more profitable, notwithstanding their effort elsewhere to depict the traffic as marginal.[11] Finally, insofar as BNSF/UP premise their approach on the need to keep their costs separate, their divisions become irrelevant, both under Board precedent and their own representations, once they decide to proceed with a joint through rate. *See, e.g., Louisville & N. R.R. v. Sloss-Sheffield Steel & Iron Co.*, 269 U.S. 217, 234 (1925); *Great Northern Ry. v. Sullivan*, 294 U.S. 458 (1935); and *Metropolitan Edison Co. v. Conrail*, 5 I.C.C.2d 385 (1989). There is thus no basis, and also no need, to accept their proposal.

Significantly, BNSF/UP make no attempt to show that the DCF results for AEPCO's ANR present any *PPL Montana/Otter Tail* cross-subsidy problems, despite

[11] BNSF/UP's claim that intermodal traffic is of marginal value to the carriers (BNSF/UP Reply at I-6) is belied by the resources that the carriers devote to attracting and servicing that traffic.

their awareness of the test.[12] Having failed to make any presentation to that effect in their Reply submission, they are barred from doing so at any later stage of the proceeding.

IX. JURISDICTIONAL THRESHOLD CONSIDERATIONS

Since the DCF analysis shows that the rates for the issue traffic should be set at the jurisdictional threshold, two issues relating to the calculation of the variable costs for the New Mexico issue traffic are particularly significant. The first issue involves whether to include the SWRR as an interline carrier, and the second issue is whether to calculate the variable costs based on the actual route of movement.

First, despite the arguments to the contrary in BNSF/UP Reply at II.A-1-3. the variable costs of the New Mexico issue traffic should be calculated without treatment of the SWRR as an interline carrier, *i.e.*, the movement should be treated as a joint BNSF/UP movement consistent with BNSF Common Carrier Pricing Authority 57966. *See* AEPCO Rebuttal at II-7-17. The SWRR is not a party to the tariff, but instead functions only as BNSF's sub-contractor. The resolution of the SWRR costing issue will thus have no bearing on the level of compensation that SWRR receives, nor will it alter what BNSF pays UP.

Furthermore BNSF's arrangement with the SWRR is intended to reduce BNSF's costs, and all available evidence shows that it serves to reduce BNSF's costs over the Rincon-Deming segment by a significant amount. However, treating the SWRR as an interline carrier has the effect of increasing BNSF's costs over that segment. A cost

[12] BNSF/UP note the *PPL Montana/Otter Tail* cross-subsidy test in their discussion of their ANR-NM and ANR-PRB in BNSF/UP Reply at III.H-5-8 & n.4.

treatment that transforms a cost-reduction arrangement into one that increases costs is arbitrary, capricious, and perverse and should not be utilized.

Moreover, the treatment proposed by AEPCO does not amount to a movement-specific adjustment. Indeed, if a movement-specific adjustment were utilized, then it would require a pass-through of the savings resulting from BNSF's arrangement with the SWRR, and AEPCO's treatment does not cause any such pass-through. In contrast, BNSF/UP's approach causes a cost-reduction arrangement to result in increased variable costs and an inflated jurisdictional threshold. AEPCO's approach plainly constitutes the best evidence of record.

Second, there is also no basis for adopting BNSF/UP's proposal, presented at BNSF/UP Reply at II.A-4 and III.H-17, to calculate the jurisdictional threshold for the New Mexico issue traffic using the ANR's longer routing via Vaughn-El Paso. *See* AEPCO Rebuttal at II-17-19 and III-H-22-23. Use of a longer routing for SAC purposes was recognized from the outset in *Coal Rate Guidelines*, 1 I.C.C.2d at 543-44, but the Board has never suggested that variable costs or the jurisdictional threshold should be based on anything other than the actual or predominant route of movement. *See, e.g.*, *WFA/Basin II* at 15.

Defendants already receive the benefit of having rates set at the higher of the jurisdictional threshold or SAC level. There is no basis on which the jurisdictional threshold should be increased by some aspect of the SAC analysis, just as there is no basis to have the SAC analysis increased by some aspect of the actual variable costs. BNSF/UP's adjustment would also contravene the statutory requirement in 49 U.S.C. §

10707(d)(1)(B) that "variable costs ... shall be determined only by using such carrier's unadjusted costs." BNSF/UP's effort to increase the jurisdictional threshold based on some aspect of the separate SAC analysis is entirely inappropriate and should not be adopted.

X. CONCLUSION

For the reasons stated above, and in AEPCO's Opening and Rebuttal submissions, the Board should order reparations and prescribe future rates for the New Mexico and PRB issue traffic at the jurisdictional threshold.

There is no basis on which to reject AEPCO's configuration of the ANR. It corresponds exactly to what the Board approved in AEPCO's prior rate case. The only change is that BNSF/UP have reversed their position from the prior rate case. However, the bulk of the ANR facilities that are used to handle the New Mexico issue traffic are also used to handle the PRB issue traffic. Moreover, BNSF/UP have made no attempt to show that any segment of the ANR as configured by AEPCO fails the *PPL Montana/Otter Tail* cross-subsidy tests. AEPCO's configuration of the ANR satisfies all of the Board's requirements. There is thus no reason to adopt, or consider further, the separate ANR-NM and ANR-PRB SARRs as proposed by BNSF/UP, because they do not, by design, comply with least-cost, most-efficient principles.

There is also no reason to require AEPCO's ANR to replicate BNSF/UP's existing interchange points for the issue traffic. Such a restriction is contrary to the flexibility on SARRs conferred by the *Coal Rate Guidelines*, the Board's rulings in AEPCO's prior rate case, and the Conference Report to the Staggers Act. AEPCO's use

of the MRL trackage rights also conforms fully to Board precedent, including decisions in AEPCO's prior rate case.

While BNSF/UP challenge a wide range of revenue, cost, design, and operating inputs to AEPCO's SAC analysis, most of their criticisms are unfounded. Under any plausible calculation of SAC, the MMM ratio would remain well below the jurisdictional threshold.

Accordingly, the Board should award reparations and prescribe rates at the jurisdictional threshold. Rates should certainly be prescribed for the PRB origins, which AEPCO has used in the past, and needs to be able and intends to use in the future, especially as there is no question that the MMM ratio will be below the jurisdictional threshold. Also, the SWRR should not be included in the calculation of the jurisdictional threshold for the New Mexico issue traffic because the SWRR functions only as a sub-contractor and its inclusion as an interline carrier would perversely cause an arrangement intended to reduce costs to have the effect of increasing cost. Finally, the jurisdictional threshold for the New Mexico issue traffic should be calculated along the actual route of movement, as there is no basis for using the SAC routing for that purpose.

Respectfully submitted,

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CERTIFICATE OF SERVICE

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